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House Subcommittee on Department Operations, Oversight, Dairy, Nutrition, and Forestry
Field Hearing: "The Future of Renewable Fuels and Flex Fuel Vehicles"
May 22, 2006

Testimony of Keith Reinholt, Field Operations Director, Michigan Soybean Association/
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Testimony of Jim Domagalski, Farmer/National Biodiesel Board Representative and
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Good morning Mr. Chairman, Ranking Member Bacca, and committee members. It is a pleasure to be here today. We appreciate the committee holding this hearing and providing the opportunity to examine this important issue.

My name is Keith Reinholt and I've been with the Michigan Soybean Association and Michigan Soybean Promotion Committee for 20 years. These organizations originally began in the 1970's by farmers throughout the state who believed that there was a need for coordinated efforts within our industry. We exist today because that need is still there, but also as important is the need for our coordinated efforts among many industries. For example our involvement with biodiesel began in the early 1990's. Biodiesel was "discovered" in part through the investment soybean farmers made in research of new products from the processed soybean. As a result, biodiesel was born and has grown rapidly for more then a decade. From our initial effort in 1992 when we literally received B100 in 5 gallon containers shipped via UPS, I have personally driven more then 500,000 miles in four diesel powered pickups fueled on biodiesel blends ranging from B2 to B20. We personally experienced how simple it is to use biodiesel. Once folks understand the simplicity of its use, they're more apt to use it too. There are little to no engine modifications and we simply splash blend the fuel.

We estimate B100 use in Michigan to have doubled each year since 2000 with an expected use in 2006 in excess of 6 million gallons. Efforts to date have resulted in biodiesel blend use by schools, county road commissions, state and national parks services, marine industry, amusement companies, municipalities, universities, state government, US Postal Service, construction and waste management companies, and more. Part of the success of such widespread use of biodiesel was an initial effort to get farmers to ask their fuel supplier to carry biodiesel in support of an American grown fuel. Doing this, as well as working with the diesel suppliers, we've helped grow the availability in Michigan to more than 110 biodiesel suppliers with 39 commercially available pumps throughout Michigan carrying various blends of biodiesel. At lease three production plants are under construction with several others in the feasibility and/or planning stages. This is truly an industry that has needed to become very coordinated and intertwined with many entities to be as successful as it is today across the nation.

The announced purpose of this hearing is to review the future of renewable fuels and flex-fuel vehicles. Renewable fuels, particularly biodiesel and ethanol, are currently experiencing tremendous growth. I would like to continue my comments this morning on the factors that have contributed to that growth for biodiesel, why this growth is important to the American people, and what must be done to keep it on its current successful trajectory.

Biodiesel is a diesel fuel replacement that is made from agricultural fats and oils and meets a specific commercial fuel definition and specification. Soybeans are the primary oilseed crop grown in the United States, and soybean oil makes up about half of the raw material available to make biodiesel. The other half consists of all other vegetable oils and animal fats. Biodiesel is made by reacting the oil with an alcohol to remove the glycerin in order to meet specifications set forth by the American Society of Testing and Materials (ASTM). Biodiesel is one of the best-tested alternative fuels in the country and the only alternative fuel to meet all of the testing requirements of the 1990 amendments to the Clean Air act.

As I've already mentioned, biodiesel is an American soybean farmer success story. After Operation Desert Storm in the early 1990's, soybean farmers struggled to maintain profitability because of high energy prices and low commodity prices. Investment in the development of a biodiesel industry was a priority to farmers eager to contribute to our domestic energy supply, while finding ways to add value to their crops. Farmers invested more than $50 million dollars throughout the 1990's to conduct research and develop biodiesel. Much of that effort focused on the testing of biodiesel to ensure performance, establish quality standards, and gain acceptance by engine and equipment manufacturers.

The biodiesel industry has shown slow but steady success since the early 90's, however, in the past two years, it has grown exponentially. In 2004 there was approximately 25 million gallons of biodiesel sales. That increased to 75 million gallons in 2005. We are currently on track to exceed 150 million gallons in 2006. Likewise, we went from 22 biodiesel plants in 2004 to more than 60 biodiesel plants currently. There are over 40 more plants currently under construction, with another 30 projects in pre-construction.

America relies on imports for 60 percent of its petroleum needs. Imported petroleum makes up the single largest component of our national trade deficit amounting to approximately one third of the total. As crude oil prices continue to rise, America's trade deficit continues to balloon. Every gallon of domestic, renewable biodiesel that is used to replace diesel fuel refined from imported crude reduces the need for imported crude and finished fuel, extends the diesel supply, and expands domestic refining capacity. Even a small reduction in demand has a positive effect on straining price pressures.

The need for increased use of biofuels has never been more pressing. Diesel fuel prices are at an all-time high. The majority of diesel fuel in this country is used in over-the-road trucks. The trucking industry serves as a critical part of our economy, and impacts every industry, business, and consumer in America. Virtually every product that we use everyday is brought to us by a diesel-powered truck. In addition, America's manufacturing sector has moved to "just-in-time" inventory systems to reduce storage and inventory costs. America's manufacturing inventory is now stored primarily in the trucks that are driving down the highway at any given time. Fuel is the single largest operational cost in the trucking industry. Average diesel fuel prices have nearly doubled over the past four years. This dramatic increase in operational cost offers enormous challenges to the trucking industry, and will be felt throughout our entire economy.

The American Trucking Association (ATA) endorsed the use of B5 as a way to supplement our nation's energy supply. Likewise, Sysco Corporation, the largest private truck fleet in the nation has begun using B5 it its trucks. Truckers often become interested in biodiesel because they would rather rely more on farmers for their fuel and less on the Middle East. However, after they begin using it, they are most often impressed by its premium fuel characteristics. Biodiesel contains oxygen so it burns cleaner, reduces smoke and smell, increases cetane, and improves lubricity. As ultra-low sulfur diesel (USLD) fuel gets phased in beginning in June of this year through June of 2007, biodiesel is well positioned to replace the lubricity that will be lost in ULSD. Diesel fuel injection systems rely on the lubricating characteristic of fuel to keep them functioning properly. Just 2 percent biodiesel can improve lubricity by as much as 65 percent.

The high price of fuel is one of the factors contributing to increased biodiesel use. However, there are three main federal policy measures that have been extraordinarily effective in stimulating biodiesel's increased production and use. Because of these three policy measures, biodiesel is beginning to make a small but significant impact on our nation's energy supply. These measures are all working extraordinarily well, but are soon scheduled to expire, and must be continued in order to keep the growth in biodiesel going strong. Although biodiesel is showing signs of success, the industry is still in its infancy, and is where ethanol was in 1982.

The first measure, the biodiesel blenders tax credit, was part of the restructured Volumetric Ethanol Excise Tax Credit or "VEETC" legislation in the JOBS Act of 2004. The new blender's tax credit for biodiesel went into effect in January of 2005. It functions similarly to the ethanol tax credit, and it has been extraordinarily effective in incentivizing the blending of biodiesel into the nation's diesel fuel supply. It has been the primary stimulant in 2005 for the dramatic increase in new plants and jobs in biodiesel, bringing economic opportunity to both rural and urban areas.

Legislation has been introduced in the Senate that includes an extension of the biodiesel blender's tax credit through 2010 and beyond. It is likely that the need for this program will go beyond 2010, but it is critical that this tax credit, which has been so effective for biodiesel, not be allowed to expire. Legislation is also currently pending in the House extending this credit through 2010 (HR 2498, Representatives Hulshof and Pomeroy).

The second policy measure that has been very effective in energizing biodiesel's growth is the Bioenergy Program. The program was initiated by the USDA in 2000 to stimulate the use of crop surpluses for energy needs. As you may recall, it was memorialized as part of the 2002 Farm Bill. However, the program is set to expire in July of this year. This program provides a production incentive which has been highly effective in the growth of the biodiesel industry. A 2005 OMB Program Assessment Rating Tool or "PART" evaluation reported that the program did an excellent job of stimulating biodiesel growth, and indicated that the program could continue to be effective for the emerging biodiesel industry. The report stated, "Increases in the production of biodiesel indicate a rise in the supply of domestically produced renewable fuels. It's also an indicator of the viability of the biodiesel industry and its expanded consumption of agricultural commodities."

High diesel prices are also hurting farmers as they have entered spring planting. Fuel is a very large operational cost for farmers. But while costs are going up, the projected value of their crop is going down. Soybean acreage in 2006 is estimated at a record 76.9 million acres, and USDA is projecting that soybean prices drop below $5.00 per bushel in 2006/07. The Food and Agricultural Policy Research Institute (FAPRI) is forecasting Marketing Loan Gains and Counter-Cyclical Payments to soybean producers of $0.72 per bushel for the 2006 crop. According to Centrec Consulting Group, if an extended 2007 Bioenergy Program for biodiesel increased soy-based biodiesel production by a very modest 40 million gallons it would be expected to increase soybean prices by a approximately $0.07 per bushel. Based on a 3.0 billion bushel crop, this increase could reduce soybean farm program outlays by up to $210 million. This would more than offset the cost of extending the Bioenergy Program for biodiesel for FY-2007. Extension of this program for biodiesel has many positives. It will be good for farmers, good for biodiesel, and will be a net plus for the US Treasury. I ask that you please consider doing what you can to extend this important program which is scheduled to expire in July of this year.

The third program that has greatly contributed to biodiesel's success is the USDA's Biodiesel Fuel Education Program. This program was additionally a part of the energy title of the 2002 Farm Bill. The program provides educational funding to support increased fuel quality measures, increased acceptance of biodiesel by engine and equipment manufacturers, petroleum partners, users, and the general public. The USDA has done a superb job in implementing this program and it has been a key ingredient to biodiesel's recent growth. A recent survey done to benchmark the program's progress showed that the public's awareness

of biodiesel rose from 27 percent in August 2004 to 41 percent in December of 2005. To impact the American public's awareness that significantly on any given issue is remarkable. In addition to greater awareness from the general public, market research shows familiarity among trucking executives increased from 27 in 2004 to 53 in 2005. Also of note:

- Four-in-five consumers continue to support a tax incentive that would make biodiesel cost-competitive with regular diesel fuel.
- 88 percent of environmental group leaders and 84 percent of health organization leaders support biodiesel as a transitional fuel, because biodiesel can make an immediate impact on reducing emissions until zero emissions technology is developed.

While the program has been highly effective, the biodiesel industry is still immature, and faces enormous challenges. Continued education is needed. I ask that you please look for ways to expand and extend this program beyond 2007.

To summarize the three federal policy measures that have been very effective in the development of the biodiesel industry and should be continued:

1) Extension of the biodiesel blender's tax credit;
2) Extension of a Bioenergy Program for biodiesel;
3) Extension and expansion of the biodiesel fuel education program.

During the 2006 State of the Union speech, President Bush outlined his Advanced Energy Initiative, which stated the goal of reducing petroleum imports from the Middle East by 75 percent by the year 2025. Biodiesel and ethanol can be the first tools used to begin reaching that goal because they are liquid renewable fuels that are available right now, ready for blending into our existing fuel supply and used in our existing vehicles. As an illustration of how biodiesel can play a role in that effort, please note that Iraq is the second largest provider of crude oil into the United States from the Persian Gulf region. Of the crude that comes from Iraq, approximately 1.85 billion gallons of diesel fuel is refined for the US market. If long-term, America were to replace just 5 percent of its 37 billion gallons of on-road diesel fuel with biodiesel, it would equal 1.85 billion gallons – the same amount of diesel fuel that we get from Iraq.

Finally, in addition to the significant benefits that biodiesel offers to increase our domestic refining capacity and overall energy supply, biodiesel offers enormous benefits to our agricultural sector. Biodiesel does much more than just utilize surplus agricultural commodities; it adds multiple layers of value to agricultural economics. There have been 5 major comprehensive economic studies evaluating biodiesel in the last 4 years. All of these studies, using different economic models, had similar conclusions: that increased utilization of fats and oils for biodiesel increases the value that farmers receive for their crops, while making protein meal cheaper as a feed for our domestic livestock producers and more competitive in international protein markets for food and feed. Not only does this allow farmers to more profitably supply global food markets, it may have the effect of increasing agricultural processing in the United States. Additional biodiesel production further increases domestic chemical processing from renewable by-products.

Mr. Chairman, members, we appreciate the opportunity to come before you today on this most critical issue. Thank you for all of the support you have given not only to the biodiesel industry, but the development of the biofuels industry overall. We look forward to continue to work with you on this important endeavor. I would be happy to answer any questions you may have.